

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
ESSKAY PICTURES CORPORATION }

Appearances:

For Appellant: Sam Katzman, its President; M. M. Ellis, Certified Public Accountant

For Respondent: Burl D. Lack, Chief Counsel;
Crawford H. Thomas, Associate
Tax Counsel

O P I N I O N

This appeal is made pursuant to Section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of Esskay Pictures Corporation to proposed assessments of additional tax in the amounts of \$123.42 and \$1,026.57 for the income years ended October 31, 1946 (taxable years ended October 31, 1946 and 1947) and October 31, 1948, respectively.

This matter is in large measure a companion to the Appeal of Sam Kataman Productions, Inc., this day decided. The comment made in our opinion in that Appeal as to the virtual absence of a statement of facts, argument and authorities in the presentation of the Appellant's position is equally applicable here.

Appellant was incorporated in this State in 1944 and engaged in the business of producing motion pictures. On September 1, 1945, it entered into a production-distribution agreement with Columbia Pictures Corporation. Under that agreement, the budget for each picture to be produced by Appellant was to be submitted to Columbia for approval. Production was to be financed by (1) a bank loan to the Appellant to the extent of 6% of production (2) an advance by Columbia to the extent of 30%, and (3) by Appellant to the extent of the remaining 10%. The agreement further provided that Columbia would distribute the pictures and after deduction of the usual distribution expenses would allocate the Appellant's portion of the receipts to the bank and itself until the loans and advances

were paid. As a security measure the productions were hypothecated, mortgaged and pledged to Columbia and it was given the right to purchase the pictures. In a sales agreement of June 8, 1948, the Appellant, which was designated as "seller," sold, assigned, transferred, and set over to Columbia all of its right, title, and interest in and to the designated motion pictures. The Appellant warranted in the, sales agreement that except as provided in Article 7 thereof it owned the full and complete title to each of the pictures. Article 7 provided that the Appellant had not transferred, assigned, or encumbered any right, title, or interest in and to any of the pictures except that it had previously sold certain pictures to Columbia, that it had mortgaged the pictures to a bank, and had granted a lien to Columbia pursuant to the production-distribution agreement of September 1, 1945.

In its returns of income for the years in question the Appellant did not report any taxable income from the distribution of pictures produced during the years ended October 31, 1946, 1947 and 1948 until it had recovered the entire cost of producing them. The Respondent, however, included in Appellant's taxable income its receipts from such distribution and allowed deductions for amortization of negative and print costs upon the basis of the ratio of gross receipts received during each period to estimated total gross receipts. Appellant objects to those adjustments on the ground that it was acting merely as Columbia's agent and received no income until such time as Columbia recouped the entire cost of the pictures. If this position be rejected, however, it contends that the amortization should be allowed on the basis of 92-1/2% of the costs for the first year and 7-1/2% thereof for the second year instead of on the gross receipts method used by the Respondent.

There is absolutely no evidence before us to justify the conclusion that the Appellant was acting as an agent of Columbia under the agreement of September 1, 1945. On the other hand, the provisions of that agreement leave no room for doubt that Appellant was regarded thereunder as the owner of the pictures it produced. In our opinion in the Appeal of Sam Katzman Productions, Inc., decided this day, we upheld the action of the Respondent in computing the allowance for amortization of motion picture film negative costs of an independent producer on the basis of the gross receipts method. No evidence, argument or authorities have been offered to us herein or in that Appeal to establish the invalidity of the Respondent's action in similarly treating film print costs. The action of the Respondent in regarding Appellant as the owner of the pictures produced under its contract with Columbia and in allowing amortization deductions for the negative and print costs is, therefore, sustained.

In the memorandum filed in support of its position the Respondent referred to its action in decreasing by \$9,253.35 the costs of two pictures sold by Appellant in the year ended October 31, 1946. Appellant had not mentioned this action in the one-page letter filed as its statement of facts and memorandum of points and authorities in this matter. At the hearing on the appeal Appellant claimed that while the Respondent had included the sales price of the pictures in Appellant's gross income; it had disallowed production costs in the amount of \$9,253.35. As Appellant was unable to present evidence concerning the costs at that time, it and the Respondent were authorized to file supplemental statements with respect thereto. Pursuant to this permission, the Respondent has filed a report indicating that the costs in question were entered upon Appellant's books as the result of bookkeeping errors and that they were not used to reduce the negative costs of other pictures. In a reply to this report the Appellant stated that the amount was used to reduce the cost of later pictures but offered no evidence or other explanation whatever in this regard. The Appellant then entered into a discussion *in* that reply relative to a **division** of profits between Columbia Pictures Corporation and itself, the former to receive 75% and it to receive 25% of the profits, but we are unable to ascertain the pertinency of this discussion to anything that **appears** in the record in this matter. In any event, the discussion does not appear to relate to the disallowance by Respondent of the costs in the amount of \$9,253.35 and the Appellant having furnished no details regarding the nature of these costs or the impropriety of the action of the Respondent with respect thereto, the disallowance of the costs and the consequent increasing of the Appellant's net income from the sale of pictures must be sustained.

O R D E R

Pursuant to the views expressed in the Opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of Esskay Pictures Corporation to proposed assessments of additional tax in the amounts of \$123.42 and \$1,026.57 for the income years ended October 31, 1946 (taxable years

ended October 31, 1946 and 1947) and October 31, 1948,
be and the same is hereby sustained.

Done at Sacramento, California, this 18th day of
December, 1952, by the State Board of Equalization.

Wm. G. Bonelli, Chairman

J. H. Quinn, Member

Gco. R. Reilly, Member

 Member

 , Member

ATTEST: F. S. Wahrhaftig, Acting
Secretary